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International Affairs

Budget function 150 covers all spending on international programs by various departments and agencies. It includes spending by the Department of State to conduct foreign relations, economic and humanitarian aid to developing countries, military and other assistance to strengthen allied nations and enhance U.S. security, radio and television broadcasting and exchange programs to promote democracy and U.S. ideals, and financing for the export of U.S. goods and services. The Congressional Budget Office estimates that discretionary outlays for function 150 will total $36.2 billion in 2005. Repayments of loans and interest income to the Exchange Stabilization Fund account for the negative amounts of mandatory spending for this function.

In the past five years, discretionary spending for international affairs grew by $14.9 billion, or about 70 percent, from $21.3 billion in 2000 to an estimated $36.2 billion in 2005. While a portion of that growth in outlays ($6.3 billion) derives from supplemental appropriations in 2003 and 2004 for the reconstruction of Iraq, most of the growth ($6.6 billion) is from three continuing commitments—to conduct foreign relations and protect U.S. diplomatic missions overseas, to strengthen coalition partners in the global wars on terrorism and illegal drugs, and to prevent the spread and treat the victims of the HIV/AIDS pandemic.

Federal Spending, Fiscal Years 2000 to 2005 (Billions of dollars)

							Average Annual Rate of Growth (Percent)	
	2000	2001	2002	2003	2004	Estimate 2005	2000-2004	2004-2005
Budget Authority (Discretionary)	23.5	24.2	25.2	33.5	49.3	30.0	20.4	-39.1
Outlays								
Discretionary	21.3	22.5	26.2	27.9	33.2	36.2	11.8	8.7
Mandatory	-4.1	-6.0	-3.8	-6.7	-6.4	-3.9	n.a.	n.a.
Total	17.2	16.5	22.4	21.2	26.9	32.3	11.8	20.0

Note: n.a. = not applicable (because all years have negative values).

150-01—Discretionary

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Eliminate the Export-Import Bank and the Overseas Private Investment Corporation

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-84	-94	-120	-152	-166	-616	-1,507
Outlays	-13	-46	-85	-126	-147	-417	-1,238

The Export-Import Bank (Eximbank) and the Overseas Private Investment Corporation (OPIC) are intended to promote U.S. exports and overseas investment by providing a range of services to U.S. companies wishing to do business abroad. Eximbank offers subsidized direct loans to private U.S. exporters, guarantees of private loans that finance those exports, and, through export credit insurance, insurance against the risk that foreign buyers will not pay for the exported goods. OPIC offers private U.S. firms subsidized investment financing and insurance against political risks. Appropriations in 2005 for Eximbank and OPIC are $132 million and $67 million, respectively.

This option would eliminate additional subsidy appropriations for Eximbank and OPIC. The two agencies could not provide new financing or issue new insurance but would continue to service their existing portfolios. Those changes would save $13 million in outlays in 2006 and $417 million over five years. In contrast, the President's budget request for 2006 would maintain funding for OPIC and would double the appropriation for Eximbank, thereby increasing spending by $25 million in 2006 relative to its level in 2005 adjusted for inflation.

The main rationale for this option is that the services those agencies provide do not on balance benefit the U.S. economy. Eximbank and OPIC finance transactions for which private firms would have trouble raising funds in private markets at private market terms. Therefore, their terms represent a U.S. government subsidy that is either retained by the U.S. company or passed on to the foreign country. That subsidy could compensate for conditions in foreign countries that might prevent U.S. firms from undertaking otherwise profitable exports and investments. For example, foreign buyers might not be able to finance imports from the United States because such loans are risky in countries that have weak debt collection systems; or foreign investments might be risky in countries that lack legal frameworks to enforce contracts. A more appropriate U.S. policy might seek to alleviate the legal and institutional problems, paving the way for broadly higher U.S. exports and more profitable foreign investment. Eximbank and OPIC, however, by guaranteeing loans and investments in countries that have not undertaken reforms, transfer to the taxpayer the same high risk that private U.S. companies now face.

An argument against this option is that the two agencies may play an important role in helping U.S. businesses, especially small businesses, understand and penetrate overseas markets. Those agencies level the playing field for U.S. exporters by offsetting the subsidies that foreign governments provide to their exporters, thereby promoting sales of U.S. goods. By encouraging U.S. investment in developing and transitional economies, those agencies may also serve a foreign policy objective.

RELATED OPTIONS: 350-04, 350-05, 350-06, and 370-03

RELATED CBO PUBLICATIONS: *Estimating the Value of Subsidies for Federal Loans and Loan Guarantees,* August 2004; *The Domestic Costs of Sanctions on Foreign Commerce,* March 1999; *The Role of Foreign Aid in Development*, May 1997; and *The Benefits and Costs of the Export-Import Bank of the United States,* March 1981

150-02—Discretionary

End the United States' Capital Subscriptions to the European Bank for Reconstruction and Development

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(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-36	-36	-37	-37	-38	-184	-386
Outlays	-19	-23	-28	-32	-37	-139	-336

The European Bank for Reconstruction and Development (EBRD) provides loans in the nations of Central and Eastern Europe and the former Soviet Union. Unlike the International Bank for Reconstruction and Development (the main component of the World Bank) and the International Monetary Fund, which lend to governments to support the reform of government policy, nearly 79 percent of the projects approved by the EBRD in 2003 represented loans to private entities. At the end of that year, the EBRD had a portfolio of more than 1,000 projects with a net value of $18.6 billion.

The United States contributed 10 percent of the capitalization of the EBRD, or $35 million, in 2005. The 2005 subscription is the last installment of an eight-year capitalization agreement with the bank. This option would terminate U.S. subscriptions to the EBRD, saving $139 million in outlays over five years, assuming that the level of U.S. support would otherwise remain steady. The President is requesting $1 million in 2006 for a final payment to the capitalization of the EBRD.

The major rationale for this option is that loans from such public entities to the private sector either displace loans that the private sector would otherwise make, in which case the program provides no additional benefit, or they represent loans that the private sector considers too risky. In the latter case, a better course for foreign assistance lies in strengthening markets and reducing creditor risk. For example, more effective frameworks for bankruptcy and debt collection would better protect creditors and encourage them to make loans that they might now consider too risky. Such reforms may be best handled through the international financial institutions that support policy reform or by grants-in-aid to foreign countries. The EBRD's strategy of making public loans to private companies without undertaking underlying reforms transfers to taxpayers risks that private investors will not take. Investments funded by private sources that respond to market conditions, including risk, are more likely to allocate capital efficiently and thereby promote economic growth.

EBRD funds are used to promote investment in a region that only recently made the transition to a market-based economy, however, and the loans provide economic support to those countries. Without institutions such as the EBRD, there could be less private investment and economic growth in the region.

RELATED CBO PUBLICATIONS: *Estimating the Value of Subsidies for Federal Loans and Loan Guarantees,* August 2004; and *The Role of Foreign Aid in Development*, May 1997

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150-03—Discretionary

Reduce Assistance to Israel and Egypt

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-614	-823	-1,032	-1,091	-1,150	-4,710	-11,395
Outlays	-572	-762	-965	-1,046	-1,117	-4,462	-11,037

As part of the 1979 Camp David peace accords, the United States agreed to provide substantial amounts of aid to Israel and Egypt to promote economic, political, and military security. That aid, which for two decades totaled over $5 billion annually for the two countries, is paid through the Economic Support Fund (ESF) and the Foreign Military Financing (FMF) program. From 1993 to 2002, Israel received an annual average of $3.1 billion. Over this time period, the ESF provided an annual average of $1.1 billion and the FMF program provided an annual average of $2 billion—although the ratio between the two began to change in 1999. Egypt received an annual average of $2.1 billion, with $770 million through the ESF and $1.3 billion from the FMF program. Those annual averages take into account the shift in ESF and FMF program funding that occurred in 1999.

In January 1998, Israel proposed phasing out its ESF payments—which up until then were $1.2 billion a year—while increasing its FMF assistance by $600 million a year. The conference report for the 1999 Foreign Operations Appropriations Act endorsed that proposal with a 10-year phase-in. As a result, it cut ESF aid to Israel by $120 million and increased FMF aid by $60 million. The conference report also reduced economic assistance to Egypt from $815 million in 1998 to $775 million in 1999—and proposed cutting it to $415 million by 2008—while keeping military aid constant. In 2005, U.S. aid to the two nations will total $4.4 billion.

This option would forgo the proposed increase in military funding for Israel (maintaining that aid at its 1998 level). The option would also continue to cut economic assistance to both Israel and Egypt each year through 2008. The reductions in Israeli aid would save $560 million in outlays in 2006, compared with this year's funding level; a total of $4.1 billion over five years; and almost $9.8 billion over 10 years. The cuts to Egyptian aid would increase total savings in outlays by $12 million in 2006, $400 million over five years, and $1.2 billion over 10 years.

Proponents of this option argue that Israel's strategic security situation has improved recently because Saddam Hussein's regime in Iraq has been destroyed; Israel has concluded a peace treaty with Jordan; and peace talks with the Palestinians and Syrians are continuing. In addition to those developments, Israel's per capita income (in excess of $19,500) approaches that of the United States' European allies, who have long been prodded by the Congress to assume greater responsibility for their own defense.

As for Egypt, some analysts say U.S. assistance to that country is not being spent wisely or efficiently. Critics note that the historical levels of appropriations have exceeded Egypt's ability to spend the funds, leading to the accumulation of undisbursed balances, inefficient use of assistance, and delays in making the reforms needed to foster self-sustaining growth. Furthermore, many other countries and organizations contribute substantial amounts of money to Egypt, which could make reducing U.S. assistance more feasible.

Opponents of this option argue that the continuing Palestinian resistance movement has placed burdens on the Israeli military and economy—particularly the tourist, construction, and agricultural sectors—and thus economic and military assistance must continue at current levels. Furthermore, some would argue that funding to Israel is important to U.S. strategic interests in terms of maintaining and strengthening ties with the region's only democracy. Opponents also argue that assistance to Egypt should be continued to help further the President's U.S.-Middle East Partnership Initiative given Egypt's important moderating role in the Israeli-Palestinian conflict.

Finally, some critics contend that if the current government in Egypt lost financial backing, the influence of anti-American fundamentalist Islamic political forces
may increase with undesirable consequences to U.S. in- 150
terests in the region.

RELATED CBO PUBLICATION: *The Role of Foreign Aid in Development*, May 1997